



# Forecast change: ECB with intermediate spurt

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**The recent noticeable fall in inflation rates and the slump in leading economic indicators have prompted us to revise our ECB forecast, especially since ECB President Lagarde gave corresponding indications today. Contrary to our previous expectations, the ECB central bankers will probably cut interest rates again in October. After a further rate cut in December, the ECB is likely to return to its slower pace from 2025 – with rate cuts in March and June. The deposit rate would then be 2.50% (previously: 2.75%).**

## Inflation rate under 2% ...

Inflation in the euro area is currently on a clear downward trend. At 2.2%, it was already only just above the ECB's 2% target in August and is likely to have fallen further in September. Most economists expect the inflation rate published tomorrow to fall to 1.8%; we see further downside risks even for this value. This is because the figures already published by some euro area countries have surprised to the downside. For example, inflation in Spain fell from 2.4% to 1.7% and in France from 2.2% to 1.5%; economists had only expected a fall to 1.9% for both countries (Chart 1). In Germany, inflation fell as expected from 2.0% to 1.8%. The main reason for the recent surprisingly low inflation is the fall in energy prices. In addition, core inflation (excluding energy, food and tobacco) should have fallen slightly from 2.8% to 2.7%.

## ... and increasing economic risks ...

In addition, the economic outlook has recently suffered a noticeable setback. The composite purchasing managers' index for the euro area fell from 51.0 points to 48.9 points in September and is therefore at a level that suggests an extremely weak economy or even a slight recession in the coming months.

## ... provide doves with arguments for interest rate cut in October

The monetary policy doves, who are in the majority in the ECB Governing Council, are likely to use the slump in leading indicators and the downward surprise in inflation to push through a further interest rate cut in October. In recent weeks, they have already expressed their concerns about the subdued economy and the possibility of inflation undershooting the 2% target. Just today, ECB President Lagarde emphasized at her **hearing** before the EU Parliament that the recent fall in inflation would be taken into account at the October meeting. There is also a high probability that inflation will rise



less in the coming months than expected in the ECB's current projection, which is why the central bankers are also likely to cut interest rates in December.

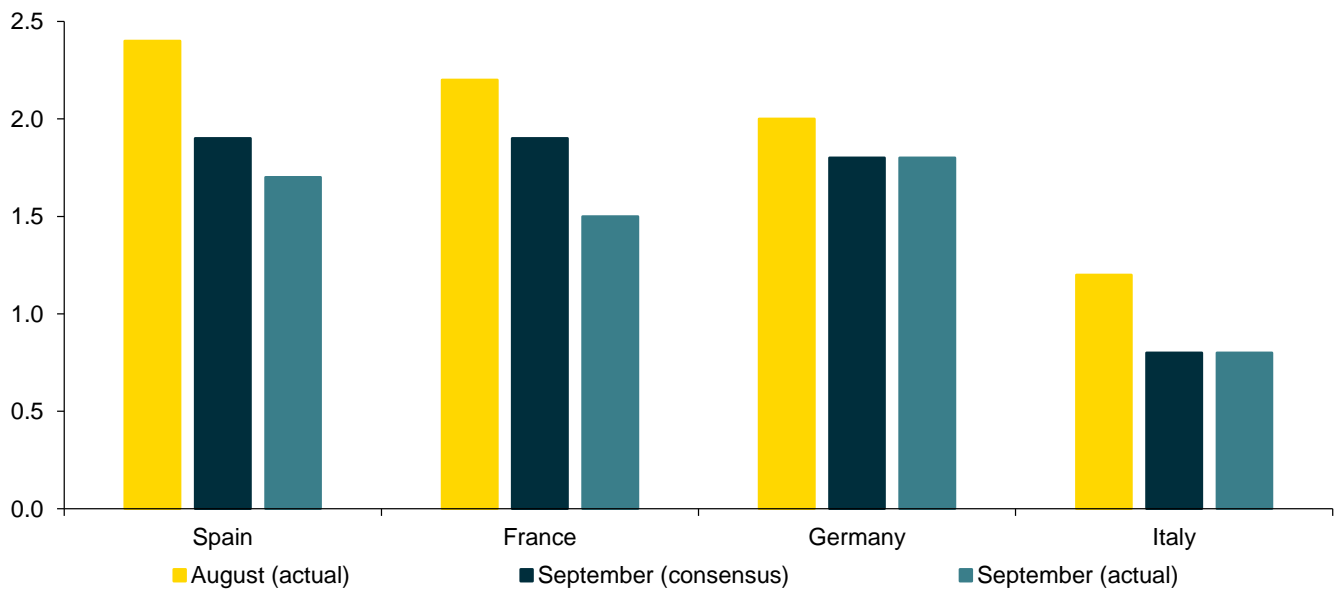
### Slower pace of interest rate cuts again in 2025

However, this faster pace of interest rate cuts is likely to be just an interim spurt. The closer the ECB moves its key interest rates to the neutral interest rate, which according to ECB analyses is between 2.0% and 2.5%, the more vigorously the hawks in the ECB Governing Council are likely to argue against rapid interest rate cuts. At the beginning of next year, core inflation is still likely to be around 2¾%, and the continued strong wage increases do not yet suggest that inflation, particularly in services, will slow noticeably in the coming months. In addition, according to an **analysis** by ECB Governing Council member Schnabel, the effect of monetary tightening on the economy is already gradually waning. Against this backdrop, the ECB central bankers are likely to return to their more cautious approach to interest rate cuts in 2025 and only take steps at meetings with new projections, i.e. once a quarter. With interest rate cuts in October, December, March and June, a deposit rate of 2.50% would be reached.

After that, the ECB is unlikely to cut interest rates any further. This is because it should gradually become apparent over the course of the coming year that inflation has not been defeated in the long term.

#### Chart 1 - Inflation surprising to the downside

Harmonized consumer price index for the large eurozone countries, percentage change on the year



Source: Bloomberg, Commerzbank Research



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